Reforming the European fiscal rules: old wine in new bottles?

Wednesday November 25th 2022
12.00 pm – 13.15 pm

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25 November 2022 – Brussels

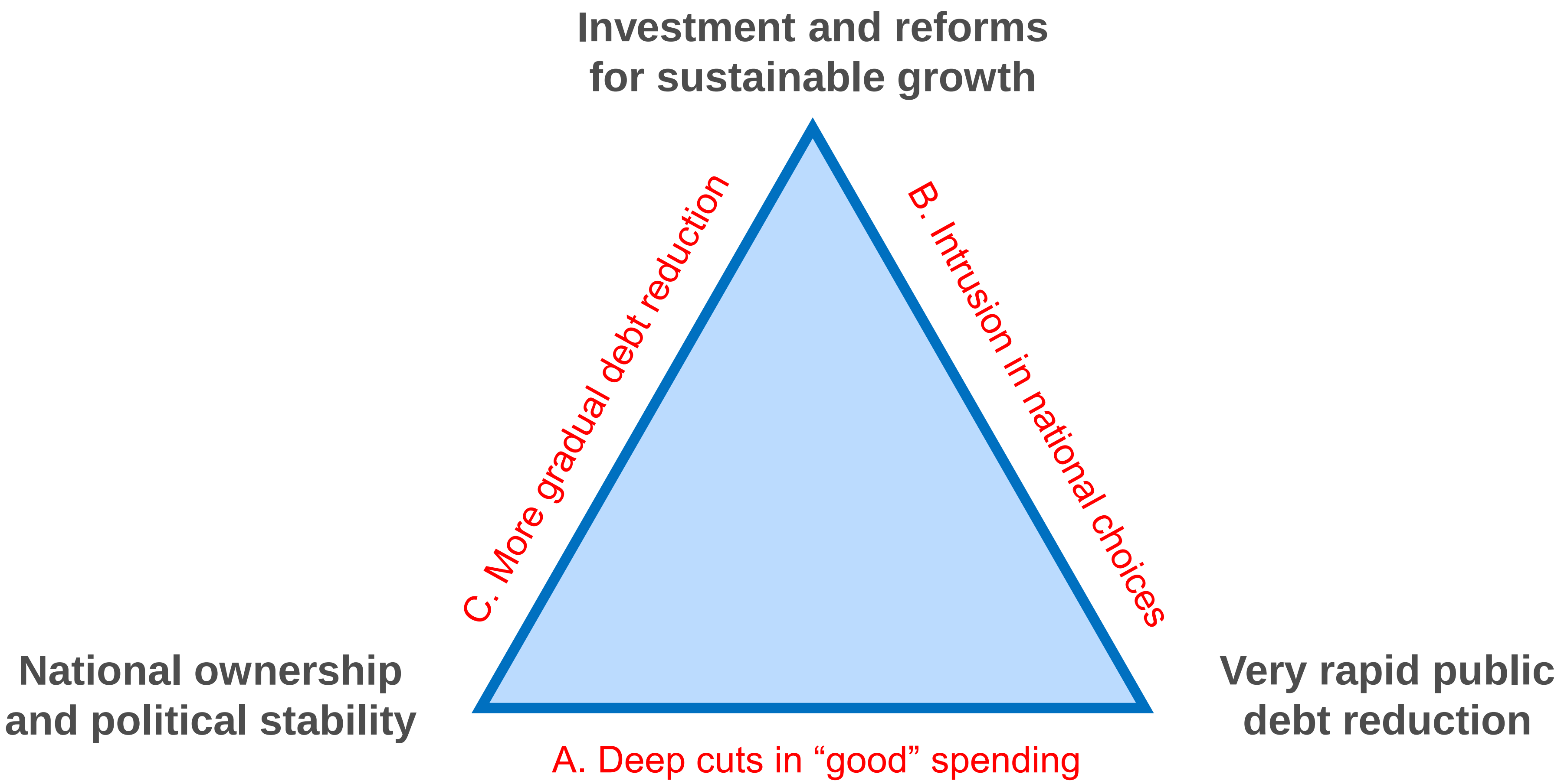
Current EU fiscal framework

Preventive arm	Corrective arm
• Anchor = Medium-term objective in structural terms • Quasi-uniform adjustment of the structural balance towards the MTO, with spending rule and structural reform and investment clauses • Significant deviation procedure	• Deficit based EDP: 3% ceiling • Debt-based EDP based on debt reduction benchmark (1/20th rule)

Problems

- **Complexity**: many indicators and rules (Structural balance, net expenditure growth, …)
- **Unrealistic pace of debt reduction** implied by 1/20th debt rule
- **Pro-cyclical bias** in good and bad times
- **Limited incentives** for reforms and investment
- **Lack of ownership**: Adjustment common across the board, ‘determined by the EU’
- **Low enforcement**: half of the MS never met the MTO. Debt-based EDP never opened.

The SGP trilemma



A suggested new fiscal framework

National ownership embedded in EU framework

0. Commission puts forward reference adjustment paths
1. Member States propose medium-term fiscal structural plans
2. Annual budgets will commit to follow the fiscal trajectory and ensure that debt will start converging to prudent levels within horizon of the plan
3. Member States can request a longer adjustment period underpinned by reforms and investments
4. Council endorsement of the plan
5. Stronger role of national IFIs

Simplification and focus on fiscal risks

1. Net expenditure path anchored on debt and agreed by Council will be the single fiscal indicator
2. Surveillance and enforcement will be risk-based
3. Debt reduction benchmark, benchmark for reduction in structural balance, significant deviation procedure and matrix of requirements no longer exist

Enforcement

1. Deficit-based EDP (3% of GDP threshold) maintained
2. Debt based EDP will be operationalised and strengthened, as a tool to ensure compliance with the agreed net expenditure path
3. Financial sanctions toolbox will be enriched with smarter sanctions
4. Macroeconomic conditionality will be maintained
5. A new tool to ensure delivery of reforms and investments underpinning gradual adjustment path

Main criticisms

- With DSA and risk analysis, the new framework is more complex than the current SGP
  >> *No, DSA only at the outset in identifying risk category and adjustment path*

- Too intrusive Commission role in deciding ‘good’ investments and reforms
  >> *No, it’s up to MS to select them, within a common framework*

- There is a risk of ‘bilateralism’, lack of transparency and unequal treatment
  >> *No, the Commission will operate within a clear common framework*

- Better keep the structural balance instead of focussing on expenditure
  >> *No, net primary expenditure is clearer, more controllable and anti-cyclical*

- Not having changed the 3%/60% imposes a deflationary bias for many years
  >> *No, after 4/7Y, the debt will continue to go down without further restrictions*

- A Central Fiscal Capacity is missing
  >> *Yes, but the reform of the fiscal rules is not the end of the game*

Next steps: to be confirmed

- Presentation and debate at the ECOFIN of 6 December 2022
- First discussion at Euro Area Summit of 15-16 December 2022 (?)
- *(Orientation for preparation of SCPs and DBPs, Q1 2023)*
- Commission legislative proposals in the first months of 2023 (?)
- *(May-June 2023 European Semester package)*
- *(Second half of 2023: repeal of General Escape Clause for 2024)*

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